

# **Expeditionary Economics in Turbulent Times**

**A Monograph  
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**AY 2011**

REPORT DOCUMENTATION PAGE				Form Approved OMB No. 0704-0188	
Public reporting burden for this collection of information is estimated to average 1 hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing this collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden to Department of Defense, Washington Headquarters Services, Directorate for Information Operations and Reports (0704-0188), 1215 Jefferson Davis Highway, Suite 1204, Arlington, VA 22202-4302. Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to any penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number. <b>PLEASE DO NOT RETURN YOUR FORM TO THE ABOVE ADDRESS.</b>					
1. REPORT DATE (DD-MM-YYYY) 29-03-2011		2. REPORT TYPE SAMS Monograph		3. DATES COVERED (From - To) June 2010 – March 2011	
4. TITLE AND SUBTITLE Expeditionary Economics in Turbulent Times				5a. CONTRACT NUMBER	
				5b. GRANT NUMBER	
				5c. PROGRAM ELEMENT NUMBER	
6. AUTHOR(S) LTC James R. Connally (U.S. Army)				5d. PROJECT NUMBER	
				5e. TASK NUMBER	
				5f. WORK UNIT NUMBER	
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) School of Advanced Military Studies (SAMS) 250 Gibbon Avenue Fort Leavenworth, KS 66027-2134				8. PERFORMING ORGANIZATION REPORT NUMBER	
9. SPONSORING / MONITORING AGENCY NAME(S) AND ADDRESS(ES) Command and General Staff College 731 McClellan Avenue Fort Leavenworth, KS 66027-1350				10. SPONSOR/MONITOR'S ACRONYM(S) CGSC	
				11. SPONSOR/MONITOR'S REPORT NUMBER(S)	
12. DISTRIBUTION / AVAILABILITY STATEMENT Approved for Public Release; Distribution Unlimited					
13. SUPPLEMENTARY NOTES					
14. ABSTRACT The United States today finds itself in a turbulent era of failing and underdeveloped states. When a population either threatens or undertakes an overthrow of their government, the government will often request United States assistance for post-conflict stabilization. Often this assistance will extend past a normal security function and into the realm of economics. This monograph explores the term expeditionary economics and the importance of contextual understanding by military planners and commanders prior to intervening in another state's economic system. Additionally, analysis of the economic development of Peru provides examples of both successful and unsuccessful economic interventions. Lessons learned from Peru's defeat of the Shining Path provide an example of how a flawed approach fueled an insurgency while a perceptive approach helped eliminate the source of grievances within a population. While these lessons will not provide a formulaic answer to conducting future expeditionary economics, such knowledge provides better judgment in how to approach future interventions. Only through contextual understanding will military commanders and planners influence a state to change laws and economic practices in order to eliminate the source of economic grievances within a population and to increase economic growth.					
15. SUBJECT TERMS Economics, History, Counterinsurgency					
16. SECURITY CLASSIFICATION OF: (U)			17. LIMITATION OF ABSTRACT  (U)	18. NUMBER OF PAGES  (U)	19a. NAME OF RESPONSIBLE PERSON Wayne W. Grigsby Jr. COL, U.S. Army
a. REPORT (U)	b. ABSTRACT (U)	c. THIS PAGE (U)			19b. TELEPHONE NUMBER (include area code) 913-758-3302

# **SCHOOL OF ADVANCED MILITARY STUDIES**

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## **Abstract**

EXPEDITIONARY ECONOMICS IN TURBULENT TIMES by LTC James R. Connally, U.S. Army, 49 pages.

The United States today finds itself in a turbulent era of failing and underdeveloped states. When a population either threatens or undertakes an overthrow of their government, the government will often request United States assistance for post-conflict stabilization. Often this assistance will extend past a normal security function and into the realm of economics. This monograph explores the term expeditionary economics and the importance of contextual understanding by military planners and commanders prior to intervening in another state's economic system. Additionally, analysis of the economic development of Peru provides examples of both successful and unsuccessful economic interventions. Lessons learned from Peru's defeat of the Shining Path provide an example of how a flawed approach fueled an insurgency while a perceptive approach helped eliminate the source of grievances within a population. While these lessons will not provide a formulaic answer to conducting future expeditionary economics, such knowledge provides better judgment in how to approach future interventions. Only through contextual understanding will military commanders and planners influence a state to change laws and economic practices in order to eliminate the source of economic grievances within a population and to increase economic growth.

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## Introduction

Since the end of World War II, many states of the world experimented with various forms of economics. Overall, the economic systems that allowed for a capitalistic approach succeeded whereas those who relied upon central planning ultimately failed. Although numerous reasons exist for the multiple failures of centrally planned economies, the overriding cause for such failures often stems from the lack of economic opportunity. Additionally, when the system of the state excludes individuals and groups from access to legitimate economic opportunities, the system drives these individuals and groups either to work outside the legal system or to take extreme actions against legitimate governments.

When violence erupts from within a populace against a government, governments often focus on eliminating the symptoms rather than the underlying causes for the violence. Military intervention initially restores some semblance of stability, but normally it fails to address the long-term catalysts of violence. During such pivotal moments, tremendous opportunities emerge to initiate economic growth through an acceptable set of economic policies. United States Army doctrine addresses the important development tasks of establishing economic policies, securing natural resources, engaging the private sector, encouraging trade, rebuilding economic governance institutions, and building essential economic infrastructure; however, it fails to discuss the tremendous issue of the exclusion of individuals and groups from legitimate economic activity.<sup>1</sup> Military doctrine acknowledges the importance of an engaged labor force, but there exists an overreliance upon intergovernmental organizations to set up economic policies and establish conditions for long-term development and investment. By relying on such entities, the United States government misses an opportunity to influence the initiation of needed economic policy changes and often fails to support lower level sectors that comprise the engine of growth.

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<sup>1</sup> *Field Manual 3-07: Stability Operations*, October 2008, 2-8 – 2-9.

According to Carl J. Schramm of the Kauffman Foundation, the United States needs to develop an ability to conduct expeditionary economics given that the current attempts at rebuilding economies after conflict or disasters fall short.<sup>2</sup> Dr. Schramm identifies that economic growth is critical to establishing social stability and attributes many of the recent failures of development economics to the shortcomings in the current doctrine on international development. He further suggests that the United States' entrepreneurial model provides an example for future expeditionary economic endeavors.

Though the term expeditionary economics lacks a universally accepted definition and few authors write concerning the topic, historical examples exist that assist in the formation of an accepted doctrine. For instance, the Peruvian government's economic development process during the 1990s provides an example of how changes in law and economic practices helped eliminate the source of grievances within a population. Lessons learned from Peru's defeat of the Shining Path provide an example that should facilitate greater understanding of the proper use of economics to support the defeat of future enemies or resurrect the economy of a country after a disaster. However, such a historical example will not provide a predictive method for future leaders and planners to apply to future problems. Rather, the understanding gained by future leaders and planners from such instances illustrates how changes to policy influenced economic systems. This knowledge provides better judgment when attempting to influence a country's economy in future post-conflict situations.

Certain development economic advocates, such as David Landes and Paul Krugman, argue that a country's confined culture, isolated geography, deficient education, unattainable finance, or undemocratic government represents the true issues experienced by faltering economies. Although extremely important, these variables are not critical elements that drive the

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<sup>2</sup> Carl J. Schramm, "Expeditionary Economics: Spurring Growth After Conflicts and Disasters," *Foreign Affairs* 89, no. 3 (May/June 2010): 89.

economy of a country. Additionally, other development economists, such as Jeffery Sachs and John Maynard Keynes, advocate for plans that either focus on rapid changes within a country's economic system or place unnecessary requirements that support a utopian or special interest goal. While many of the changes support a commonly desired outcome, tremendous or unnecessary changes to a system often cause it to fail and revert to a more centrally controlled economy.

A state's economic system exists in a vulnerable and sensitive condition. Prior to entering a conflict, consideration of the state's post-conflict economy must take place. Therefore, when approaching another state's economic system, planners and commanders must approach another country's economic system with extreme caution. Military commanders and planners must concentrate on understanding the environment in order to successfully influence the state's economy. Most environments require understanding four essential areas. First, commanders and planners must possess a deep understanding of the successes and failures of past economic development attempts to improve the domestic economic system of the state. Second, commanders and planners must understand the need to suppress the appetite for immediate changes to a country's economic system. This requires extreme patience and a long-term view of influencing the economic system of another country to reach an acceptable outcome of a new form of capitalism that facilitates access to its people. Third, commanders and planners must understand that the complexity of dealing with an economic system cannot be solved through simple solutions or a large central plan. Fourth, commanders and planners must understand the historical background of the area, cultural issues, economic systems, and the legal difficulties that facilitated the specific grievances. Through contextual understanding, commanders and planners can influence a state to change laws and economic practices in order to eliminate the source of economic grievances within a population and to increase economic growth.



## Structure

This monograph does not examine the appropriateness of the United States military conducting expeditionary economics. Rather, the monograph examines the difficulties of intervening in the economics of another state and the importance of contextual understanding when performing expeditionary economics. This monograph is arranged in five major sections. The first section provides background on development economics and relevant history of Peru. The second section discusses the rise of the Shining Path. The third section examines the causes of the legal and extralegal activities. The fourth section provides analysis on development economic successes and failures. Finally, the fifth section provides essential areas for military commanders and planners to focus upon when conducting expeditionary economics.

## Expeditionary Economics Defined

The term expeditionary economics does not possess a universally accepted definition. However, one may analyze the term's meaning by disassembling it, defining the individual words, and reassembling the term to create a suitable meaning. *Expeditionary*, as defined by the Oxford English dictionary, means "of or forming an expedition, especially a military expedition."<sup>3</sup> Additionally, the Oxford English dictionary defines *economics* as a noun, meaning "the branch of knowledge concerned with the production, consumption, and transfer of wealth."<sup>4</sup> After reducing the term to its basic elements, one may begin to understand the term's true meaning. Adding *expeditionary* to the word, *economics*, gives the term a military connotation – that is when a military is deployed to a foreign country. Although expeditionary economics intertwines itself with the military, the focus of this type of economics sounds comparable to the field of

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<sup>3</sup> *Oxford Dictionaries*, [http://www.oxforddictionaries.com/view/entry/m\\_en\\_us1245619#m\\_en\\_us1245619](http://www.oxforddictionaries.com/view/entry/m_en_us1245619#m_en_us1245619) (accessed August 31, 2010).

<sup>4</sup> *Oxford Dictionaries*, [http://www.oxforddictionaries.com/view/entry/m\\_en\\_us1243059#m\\_en\\_us1243059](http://www.oxforddictionaries.com/view/entry/m_en_us1243059#m_en_us1243059) (accessed August 31, 2010).

development economics. Therefore, for the purposes of this monograph, the term expeditionary economics defines a type of economics similar to development economics that a military performs or supports when they intervene in another country's economic system.

## **Background on Development Economic Approaches**

The field of economics contains almost as many economic theories as it does economists. This paper does not examine the debate between various economic theories such as how world markets have emerged from the Keynesian system of macroeconomic policies to the Chicago School of economics promoting free markets. Rather, the monograph centers on the ill-defined term of expeditionary economics and associating that term to existing economic thought. Since the field of development economics encompasses a comparable type of economics to the concept of expeditionary economics, an examination of development economics will prove helpful.

Development economics focuses on economic growth, but consists of two very different approaches in developing a country's economic structure. First, the top-down approach, focuses primarily on policy changes performed by the central government. Secondly, the bottom-up approach supports the local individuals or groups. Both have their bevy of vocal advocates, yet, neither extreme has produced successful changes within any country in recent history.

Some economists fervently argue that successful examples of intervention exist. However, most examples consist of the post World War II Japanese and German recovery and the resulting successes of the Marshall Plan. Unfortunately, both of these examples are not true instances of expeditionary economics or even radical economic intervention. In fact, many individuals fail to understand that the Marshall Plan focused on reindustrialization instead of financial planning.<sup>5</sup> Prior to the war, the German and Japanese governments possessed advanced

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<sup>5</sup> Erik S. Reinert, "Increasing Poverty in a Globalized World: Marshall Plans and Morgenthau Plans as Mechanisms of Polarization of World Incomes," In *Rethinking Development Economics*, edited by Ha-Joon Chang (London: Anthem Press, 2003), 455.

economies. During the post-conflict period, both economies were reconstructed by their own citizens and not by Americans or a big American plan.<sup>6</sup> Without these two highly touted examples of development economics, the argument for intervening with a big plan falls short. Additional examples of successful economic interventions by another state do not readily exist. Yet, the fact remains that when states fail, and the United States government possesses enough interest to intervene, the intervention will require the United States government to normally call upon its military to intercede. Post-conflict intervention requires the military to provide security, support governance, and supply economic assistance.

However, such intervention causes a great deal of concern among many Americans. In the field of economics, economists, such as William Easterly, believe that “military intervention to overthrow evil dictators and remake other societies into some reflection of Western democratic capitalism is the extreme of contemporary utopian social engineering.”<sup>7</sup> However, the failing state will, nevertheless, request the visiting state’s military to begin developing the state’s economy. The military normally enters the failing country first, possesses the greatest ability to plan, and maintains the largest amount of manpower within a foreign country. As a result, the burden to prevent the country from slipping into economic chaos, falls directly on the visiting state’s military. Consequently, with an understanding of the complex nature of an economic system within a state, military leaders and planners must carefully determine the best approach to the situation. Although planners do not have a wealth of examples from which to choose, they can analyze Peru as a case study in both a successful and unsuccessful intervention. Peru provides an excellent example of a country that possessed both civilian and military leadership, experienced a Maoist insurgency within its borders, struggled with economic solutions, and

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<sup>6</sup> William Easterly, *The White Man’s Burden: Why the West’s Efforts to Aid the Rest have done so much Ill and so Little Good*, (London: Penguin Books Ltd., 2006), 345.

<sup>7</sup> Easterly, 14-15.

eventually succeeded in forming acceptable solutions that eliminated many economic grievances and prevented an insurgency from flourishing within its borders.

## **Economic Background on Peru**

Outsiders may never fully understand the nuances of any society, however, if one is to influence the economy of another state, it is essential to understand the background of the state, its economy, its politics and its people. In the case of Peru, although insiders attempted for decades to correct the economic azimuth of Peru, it was not until the 1990s that Peru set a course to truly provide economic opportunity for its people. Peru possesses a rich and diverse political and economic history. Once known as the cradle of the Incan civilization and the center of Spain's Empire in South America, Peru was one of the last Latin American countries to gain its independence from Spain. While Peru experienced almost 300 years of Spanish rule and gained its independence in 1824, it was not until 1895 that a stable elected civilian government was formed with the establishment of the "Aristocratic Republic."<sup>8</sup> Prior to the Aristocratic Republic's establishment, the leadership of Peru simply continued many of the colonial systems inherited from Spain. Although the Aristocratic Republic enacted many changes, the Peruvian government continued two main elements of Spanish control: authoritarian political institutions and mercantilist economic institutions.<sup>9</sup>

Authoritarian rule continued until 1895 and Peru maintained mercantilist economic policies with Great Britain. Consequently, many emerging Peruvian entrepreneurs acted as agents for British interests.<sup>10</sup> Many of these entrepreneurs became the elites within Peruvian society and exerted influence to protect their interests and exclude competition. Political leaders

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<sup>8</sup> David Scott Palmer, "Introduction: History, Politics, and Shining Path in Peru," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 1.

<sup>9</sup> Palmer, *The Shining Path of Peru*, 4.

<sup>10</sup> Ibid., 5.

attempting to change the status quo did not last. In fact, few leaders lasted to serve a full term. Although there were some enlightened military leaders such as Ramon Castilla (1845-1851, 1854-1862), who worked to change the existing system, Peru's political divisions did not arise from a typical conservative-liberal split (like much of Latin America during the nineteenth century), but more by the issue of military or civilian rule.<sup>11</sup> Regardless of the party controlling the politics, mercantilist economic practices remained relatively untouched by the various governments. Such economic practices led to the economic difficulties within Peru.

Throughout Peru's history, the mercantilist economic system oppressed most Peruvians rather than communism or democratic capitalism. The Peruvian experience with mercantilism is an important aspect of Peruvian society that spanned from Peru's time as a Spanish colony to the 1990s. Peruvian economist, Hernando de Soto, defined mercantilism "as the supply and demand for monopoly rights by means of laws, regulations, subsidies, taxes, and license."<sup>12</sup> In other words, within Peruvian society, there existed state-sanctioned monopolies that protected the few from the competition of the many. Although most western states engaged in mercantilist economic practices until the late 1700s, some nations, like Peru did not undergo the economic evolutions that developed nations experienced. In fact, whether Peru's colonial heritage or to the lack of a destabilizing attack upon the central government, mercantilism lasted in Peru at least a century longer than in Europe. However, after World War II, an emergence of informal activity, frequent property invasions, widespread lawbreaking, the first elements of a market economy, the anarchy resulting from negotiating for laws and bureaucratic favors, and many of the factors that

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<sup>11</sup> Ibid., 7.

<sup>12</sup> Hernando de Soto, *The Other Path: The Economic Answer to Terrorism* (New York: Basic Books, 1989), xx.

preceded and shaped the European Industrial Revolution occurred that fought the restraints of a mercantilist economy.<sup>13</sup>

Prior to World War II, Peru's mercantilist economic policies did not appear to harm the state's economy or stability. Throughout the majority of the 1800s, Peru enjoyed an economic expansion spawning from an abundance of natural resources (especially the extremely large and rich deposits of guano on islands off the coast). However, Peru's economic tide contracted with the outbreak of the War of the Pacific (1879-1883). Although this war with Chile resulted in Peru's defeat that humiliated and demonstrated the weakness of the Peruvian government, and caused the loss of the coastal department of Tarapaca (with its immense nitrate deposits) to Chile, the war successfully ushered in a period of social and political change under a limited civilian democracy.<sup>14</sup> However, economically, the war was a disaster for Peru. It increased Peru's economic dependency on foreign markets, foreign entrepreneurship, and foreign loans. It also "set the pattern for a limited state (i.e. small budgets) and private enterprise (i.e., large foreign investment) that most Peruvian governments tried to follow until the 1968 military coup."<sup>15</sup>

Although the War of the Pacific caused Peru to lose a significant portion of its economic resources, the war did not change Peru's overall economic system. Peru's political leaders dealt with the challenges of balancing the desires of the military and the elites. In the war's aftermath, the elites and the military concentrated on maintaining the status quo. As the only elected civilian to complete a full term between 1914 and 1984, Manuel Prado (1939-1945; 1956-1962) was one of the few Peruvian leaders able to maintain the status quo and satisfy the desires of both the

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<sup>13</sup> de Soto, *The Other Path*, 235.

<sup>14</sup> Palmer, *The Shining Path of Peru*, 5.

<sup>15</sup> Ibid., 7.

elites and the military. Prado accomplished this difficult task by being a part of the elite and by providing the military with the desired military and budgetary requirements.<sup>16</sup>

Economic difficulties continued to plague Peru. However, it was not until Peru began to experience the post WWII migrations to urban areas and the emerging problems with the mercantilist economic system, that caused the government to recognize the need for reform. The majority of the reforms focused on integrating labor, students, and the more marginal middle sectors. Although the government initiated many important reforms between 1963 and 1968, the failure to fully carry out any reform initiatives and meet the development challenges in the 1960s, caused the military to intervene on October 3, 1968 with a bloodless coup.<sup>17</sup>

The military's control over the Peruvian government marked a pivotal time in the state's history. For the first time, the state's leadership focused on reforming the state and not on maintaining the status quo. Remarkably, the military looked to create changes that supported the majority of Peruvians. The reforms concentrated on diversifying its economy to reduce the country's economic and political dependency and institute large-scale agrarian reforms to eliminate large private landholdings. The policies did not try to redistribute the existing share of the market. Rather, it focused on generating economic growth, improving the distribution of this growth, and garnering the support of economic elites to redirect their wealth toward new productive activities.<sup>18</sup> However, established laws and economic practices did not always support the changing reality occurring at the grass-roots level. Individuals emerged from rural areas and had to work outside the law to engage in activities normally accepted by formal society in other states. This behavior revealed that Peru could no longer follow a mercantilist economic path.

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<sup>16</sup> Palmer, *The Shining Path of Peru*, 9.

<sup>17</sup> Ibid., 11.

<sup>18</sup> Ibid., 12.

Many of the reforms focused on directing the economic evolution away from mercantilism. General Velasco Alvarado's agrarian reforms in the 1970s helped to dismantle the socio-economic system that dominated and isolated the rural population.<sup>19</sup> However, the military's inability to quickly adapt to both Peru's evolving internal problems and those within the global economy increased discontent and dissatisfaction among the people. By 1977, mounting economic and political pressures prompted the military regime to initiate a gradual return to civilian rule.<sup>20</sup> The return to civilian rule corresponded to the Shining Path's people's war on the eve of the national election of May 18, 1980.<sup>21</sup>

During the 1980s, Peru witnessed increasing terrorist violence and continued economic strife. In many cases, the government's action only exacerbated problems and increased the hardships on the Peruvians. However, many outside agencies share the blame with the Peruvian government. During the debt crisis of the 1980s, the IMF and World Bank possessed a great amount of leverage over developing countries and instituted many policy requirements and conditions that were not generally in the interests of the developing countries.<sup>22</sup> For example, the International Monetary Fund (IMF) imposed onerous, restrictive and controversial requirements on the domestic economic policies. These restrictions crippled Peru's eligibility to receive new external resources and debt refinancing.<sup>23</sup> Although Peru made such required changes, Peru continued to experience economic woes and terrorist violence. Such hardships led a majority of Peruvians to crave dramatic change away from what the traditional political parties had to offer

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<sup>19</sup> de Soto, *The Other Path*, 232.

<sup>20</sup> Palmer, *The Shining Path of Peru*, 13.

<sup>21</sup> *Ibid.*, 14.

<sup>22</sup> Martin Khor, "Globalization, Global Governance and the Dilemmas of Development," In *Rethinking Development Economics*, edited by Ha-Joon Chang (London: Anthem Press, 2003), 533.

<sup>23</sup> Palmer, *The Shining Path of Peru*, 14.



and to gamble on an individual that would represent a “new Peru.”<sup>24</sup> In June 1990, a relatively unknown politician, Alberto Fujimori, won the Peruvian national election by running on a platform focusing on alleviating economic hardships and eliminating guerilla violence.

During the campaign, Fujimori’s platform was not as extreme as his challenger’s, Vargas Llosa. However, once in power, Fujimori immediately initiated an economic shock program even more severe than Llosa proposed during his campaign. This economic shock program (known as “Fujishock”) implemented drastic measures which dramatically accelerated inflation, further reduced domestic economic activity, and pushed several million more Peruvians below the poverty line (approximately 14 million, or 60 to 70 percent of the population).<sup>25</sup> Fujimori implemented such draconian measures in an attempt to reestablish international credit and create a foundation for future economic growth. Throughout this period, the Washington Consensus heavily influenced many of the policies Fujimori implemented.

American economist John Williamson initially coined the term Washington Consensus to describe a set of economic policies imposed by the World Bank and the International Monetary Fund during the 1990s.<sup>26</sup> The Washington Consensus established a list of ten specific macroeconomic policy prescriptions for developing countries to implement in order to recover from the economic and financial crisis of the 1980s. The policy prescriptions outlined in the Washington Consensus became synonymous with neo-liberalism and centered on trade liberalization, liberalization of inflows of foreign direct investments, deregulation and privatization.<sup>27</sup> Economists and policymakers alike consider this a controversial list as it requires

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<sup>24</sup> Patricia Oliart, “Alberto Fujimori: ‘The Man Peru Needed?’,” In *Shining and Other Paths: War and Society in Peru, 1980-1995*, edited by Steve J. Stern (Durham: Duke University Press, 1998), 412.

<sup>25</sup> Palmer, *The Shining Path of Peru*, 14.

<sup>26</sup> Erik S. Reinert, *How Rich Countries Got Rich and Why Poor Countries Stay Poor* (New York: PublicAffairs, 2007), 47.

<sup>27</sup> *Ibid.*, 204.

adherence to a set of rules instead of allowing the state to find its own path to development and reform. The ten macroeconomic policy prescriptions are: 1) fiscal discipline, 2) redistribution of government funds on the basis of need rather than politics, 3) broadening of tax bases and reduction of marginal tax rates, 4) liberalization of financial markets (absence of entry and price controls for institutions, national treatment for foreign firms, and absence of capital controls), 5) competitive exchange rates, 6) replacement of trade quotas with tariffs, 7) removal of barriers to product market competition, 8) privatization of state-owned enterprises, 9) abolition of barriers to foreign direct investment, and 10) strong and effectively enforced property rights.<sup>28</sup>

Although extremely painful for Peru, Fujimori's "Fujishock," with the inclusions of select Washington Consensus prescriptions, began to turn the economy around. However, since Fujimori lacked a congressional majority and did not desire to continue negotiating through democratic channels, on April 5, 1992, he temporarily suspended democracy by suspending the Peruvian congress, the judiciary and the constitution.<sup>29</sup> This autoglope (coup against oneself) received domestic and international condemnation, however Fujimori easily continued to effectuate reforms. The autoglope only lasted until December 1992, during which, Fujimori facilitated economic stabilization and centralized, thus increasing, the power of the presidency.<sup>30</sup> The success of market-oriented economic policies coupled with the capture of the Shining Path's leader, Abimael Guzman, in late 1992 set the Peruvian state on an excellent economic path and permitted Fujimori to bring together the technocrats, business elites and personal loyalists to collaborate on economic reforms.<sup>31</sup> The lasting effects of the economic reforms within Peru are

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<sup>28</sup> William J. Baumol, Robert E. Litan, and Carl J. Schramm, *Good Capitalism, Bad Capitalism, and the Economics of Growth and Prosperity* (New Haven: Yale University Press, 2007), 55.

<sup>29</sup> Carol Wise, *Reinventing the State: Economic Strategy and Institutional Change in Peru* (Ann Arbor: The University of Michigan Press, 2003), 179.

<sup>30</sup> Moises Arce, *Market Reform in Society: Post-Crisis Politics and Economic Change in Authoritarian Peru* (University Park: The Pennsylvania State University Press, 2005), 39.

<sup>31</sup> *Ibid.*, 41.

still in question. However, early indications suggest that Fujimori's approach set Peru on a sustainable development path.

## **The Shining Path**

The violence in Peru, between the years of 1980 and 1993, claimed over 30,000 lives and resulted in more than 24 billion dollars in direct and indirect property damages (over half of Peru's Gross National Product).<sup>32</sup> Many reasons for social discontent existed in Peru during this time. However, the dissatisfaction with Peru's government does not explain the rise of one of the most brutal insurgencies in the Western Hemisphere. While Peru faced many of the same difficulties of other Latin countries, how did a young philosophy professor named Abimael Guzman, create the violent organization known as Sendero Luminoso, or the Shining Path?

### **Origins of the Shining Path**

To understand the Shining Path, one must start at the genesis of the organization. The origins of the Shining Path began in 1959 when Abimael Guzman joined the Peruvian Communist Party (PCP). Guzman further developed the organization in 1962 when he took a job at the newly reopened San Cristobal de Huamanga University in Ayacucho, Peru.<sup>33</sup> Both the Andean department of Ayacucho and the Huamanga University were instrumental in the growth of the Shining Path. In this remote, poor and backward Andean region, Huamanga University provided the only school for higher learning and represented a path of upward mobility. This institution gave hope of an education to a people where until midcentury, bankrupt landowners persisted in the serf-like exploitation of "their" Indians.<sup>34</sup> As with many universities around the

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<sup>32</sup> Palmer, *The Shining Path of Peru*, 2.

<sup>33</sup> Cynthia McClintock, *Revolutionary Movements in Latin America: El Salvador's FMLN and Peru's Shining Path* (Washington: United States Institute of Peace Press, 1998), 262.

<sup>34</sup> Carlos Ivan Degregori, "The Origins and Logic of Shining Path: Two Views," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press 1994), 52.

world, students at Huamanga University began to question their previously held beliefs. Inequalities observed outside the campus coupled with the economic reality that few jobs existed for recent graduates caused students to protest government policies and form various political groups. Although the PCP existed at Huamanga University, Guzman formed a Red Faction group within the party. He further aligned this group with the Maoist followers that eventually created a split within the PCP between pro-Soviet and Maoist followers.<sup>35</sup>

When examining his background, Guzman's path toward leading the Shining Path does not seem predestined. However, Guzman's experiences of organizing, debating, and political infighting while at the university prepared him to create and lead the Shining Path. Additionally, Guzman gained other valuable experiences from outside Peru. Although Guzman's Maoist PCP did not support the 1965 pro-Cuban, communist insurgency within Peru, Guzman's arrest appeared imminent nonetheless. Consequently, the PCP sent Guzman to cadre school in China where he gained valuable experience.<sup>36</sup> After an enlightening time in China, Guzman returned to a changed Peru. The government takeover by the Peruvian military concerned Guzman and many of the pro-Chinese communists since the military desired to implement many of the reforms advocated by the Peruvian left winged parties. Guzman and the pro-Chinese communist strongly opposed the military government for they feared being forced out if the military succeeded in such reforms.<sup>37</sup> However in 1970, Guzman was expelled from the Maoist PCP after an internal struggle within the party. Guzman's expulsion provided a path on which the Red Faction would travel towards becoming the Communist Party of Peru – The Shining Path.<sup>38</sup> From this point

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<sup>35</sup> Ibid.

<sup>36</sup> Gustavo Gorriti, "Shining Path's Stalin and Trotsky," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 174.

<sup>37</sup> Gorriti, *The Shining Path of Peru*, 175.

<sup>38</sup> Degregori, *The Shining Path of Peru*, 53.

forward, the Shining Path's identity and belief system spawns from the mind of one person, Professor Abimael Guzman Rynosos.

## **Shining Path's Maoist Approach**

Although Abimael Guzman claimed that his ideology was the "fourth sword of Marxism," his actions were overwhelmingly Maoist.<sup>39</sup> Like Mao, Guzman identified three key phases of guerrilla war: "defensive," "equilibrium," and finally, "offensive."<sup>40</sup> Additionally, in Maoist tradition, and in order to justify armed insurgency, Guzman defined Peru's society as semifeudal and semicolonial.<sup>41</sup> Although Peru's society did not fit neatly within this Maoist construct, such a view enabled Guzman to define his approach. Guzman believed that he had to start the war from the rural base with the aid of peasants. Once he created the revolutionary base in the rural areas, Guzman believed that he would have enough forces to then encircle the cities. However, Guzman's dogmatic insistence on this misguided approach lasted until the Shining Path's first congress in 1988, where the Maoist prioritization of the countryside was modified to one focused on the cities.<sup>42</sup>

While many reasons exist to explain this misguided approach, the primary reason for the failure of this approach originates from Guzman's inflexible adherence to a guerilla model and his lack of understanding of the situation in Peru. The Shining Path did not start out as a peasant rebellion, but was derived from the university.<sup>43</sup> In fact, one of the first groups that the Shining Path recruited came from teachers and students. Although many of these individuals were the

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<sup>39</sup> McClintock, *Revolutionary Movements in Latin America*, 65.

<sup>40</sup> Ibid.

<sup>41</sup> Gorriti, *The Shining Path of Peru*, 176.

<sup>42</sup> McClintock, *Revolutionary Movements in Latin America*, 65-66.

<sup>43</sup> David Scott Palmer, "Conclusion: The View From the Windows," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 262.

first in their family to receive an education, economic struggles had led many not to be able to provide for their families' basic needs.<sup>44</sup> Additionally, not until the late 1980s, did Guzman comprehend the difficulties experienced by peasants migrating to the cities. Prior to that time, Guzman viewed Peru as a larger example of what he witnessed in the Peruvian state of Ayacucho.

## **Building Political Base**

In the 1970s, Guzman started building his base in Ayacucho. This time period in Ayacucho heavily influenced the Shining Path and caused the leadership to form many of its ideals around problems facing Peru with what was seen within Ayacucho: poor, provincial, isolated, and Indian.<sup>45</sup> This experience, coupled with the influences of Guzman's stay in China, led to the Shining Path ideology's three key elements: (1) characterization of society as "semifeudal," implying that the peasantry will be the primary social base of the revolution and that democracy is impossible; (2) the fundamental role of political violence in the revolutionary process; and (3) Gang-of-Four Maoism as an invariable truth.<sup>46</sup> Although Guzman garners support through the addressing of grievances, the extreme nature of this form of communist ideology created future difficulties for the Shining Path.

When the military government was in power, the Shining Path garnered considerable sympathy and support among the Ayacucho population by addressing grievances that the military initially raised when first assuming power.<sup>47</sup> However, the military did not see the importance of some of Peru's rural departments since such areas did not typify the main issues that the central

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<sup>44</sup> McClintock, *Revolutionary Movements in Latin America*, 14.

<sup>45</sup> Palmer, *The Shining Path of Peru*, 20.

<sup>46</sup> Cynthia McClintock, "Theories of Revolution and the Case of Peru," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 247.

<sup>47</sup> Tom Marks, "Making Revolution with the Shining Path," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 215.

government faced. The central government concentrated on problems generated by large urban populations and the massive migration to urban areas. Therefore, the Shining Path took advantage of the government vacuum in Ayacucho, addressed the people's needs and consequently, garnered their support. The lack of government focus and inability to exert control in many of the rural areas helped support the Shining Paths' ideology and plan for Peru's future. The Shining Path's leadership created a strategy that initiated a People's war in order to gain control of the countryside for the purpose of encircling the cities.<sup>48</sup>

While the Shining Path grew in strength in areas where the government held little influence, they continued to struggle outside of their home base of Ayacucho. In order to compensate for its weakening impact on society, the Shining Path built increasingly well-organized cadres steeped in the ideology of destroying society in order to build a new society.<sup>49</sup> Subsequently, when the deteriorating economic conditions forced down the wages on which many peasants depended, and continued lack of access to land for economic security pressed them further, the Shining Path possessed a ready stable of hardened believers to move into other areas to reinforce the organization. The Shining Path simply transformed the power structure with itself at the top and with the peasant masses, which it considered in need of leadership and instruction, at the bottom. The Shining Path admonished villagers to refrain from participating in the capitalistic market and to remain autonomous.<sup>50</sup> During this period, the local realities of the peasant economy served to maintain sympathy for the Shining Path.<sup>51</sup> Such sympathy helped to subvert the reforms the military government often attempted. The initial actions were all political

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<sup>48</sup> Marks, *The Shining Path of Peru*, 215.

<sup>49</sup> Ibid., 213.

<sup>50</sup> Billie Jean Isbell, "Shining Path and Peasant Responses in Rural Ayacucho," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 90.

<sup>51</sup> Palmer, *The Shining Path of Peru*, 23.

until the eve of the elections in 1980, when the Shining Path's leadership decided that the time was ripe to introduce the military arm of their movement.

The Peruvian government did not take seriously the Shining Path's initial disruptions. Interestingly, the government's response, or lack thereof, caused problems with the local population. It angered the local population, when, in December 1982, the government used massive and indiscriminate military force, instead of selective force, against the Shining Path.<sup>52</sup> The Shining Path continued to exert themselves and increased their strength where the government was weak. The Shining Path established a foothold in areas where coca eradication caused ill-will and created a financial windfall for the organization, providing millions annually.<sup>53</sup> Any place where the government lacked power and influence only created more opportunity for the Shining Path. The Shining Path acknowledged this opportunity in their 1986 war plan by starting to title land, homes and businesses throughout Peru to win the favor of the people.<sup>54</sup> The Shining Path experienced immense support when they focused on the grievances of people. However, the Shining Path failed when they attempted to impose a set of procedures and controls that appeared to exert the same structures of domination most local communities were trying to escape. Interestingly, this helped individuals conclude that the government, not the Shining Path, could better respond to their needs.<sup>55</sup>

## Sources of Grievances

Grievances are often caused when groups are excluded from legitimate activities. The Shining Path failed to provide the spark to enflame Peru into a true revolution. This failure stemmed from a flawed ideology and lack of understanding concerning the grievances held by

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<sup>52</sup> Palmer, *The Shining Path of Peru*, 269.

<sup>53</sup> Marks, *The Shining Path of Peru*, 218.

<sup>54</sup> de Soto, *The Other Path*, xxiv.

<sup>55</sup> Palmer, *The Shining Path of Peru*, 22.



most Peruvians. In Peru, exclusion from the formal legal system, land disparity, and lack of access to education were the three major sources of grievances. These grievances caused the disenfranchised to search for other sources for relief, which, in turn, undermined any existing support for the local government. As Peruvians migrated from rural areas, seeking a better life, they had to rely on their entrepreneurial abilities to earn a living. This group of entrepreneurs worked in the informal or extralegal sector and made up sixty to eighty percent of the population.<sup>56</sup> These entrepreneurs desired to live under the rule of law in order to have their homes and businesses recognized. However, when they existed outside of the rule of law, in the extralegal sector, their security could only be assured through an extralegal arrangement not recognized by legitimate law. Extralegal arrangements produce many difficulties for the entrepreneur. Primarily, by not having their assets within the legal system, these entrepreneurs could not use the assets to guarantee credit, and thus did not possess any incentives to initiate long-term projects.<sup>57</sup>

The disparity of legal land ownership continued as a source of grievance for many Peruvians. Historically, the Peruvian elites drove many indigenous people from their lands so that the elites could establish large haciendas.<sup>58</sup> Although the government recognized the disparity of land as a legitimate grievance, rising population growth and the state's failed agrarian reforms only increased the divide. Land reform solutions came from a grass-roots level, but unfortunately the state failed to acknowledge the legitimacy of such solutions and dismissed the power of reforms originating from the local level. The state's failure to incorporate a grass-roots

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<sup>56</sup> de Soto, *The Other Path*, xvii.

<sup>57</sup> de Soto, *The Other Path*, xix.

<sup>58</sup> McClintock, *Revolutionary Movements in Latin America*, 167.

movement for land reform coupled with an imposition of a bureaucratic cooperative structure, created cooperatives that lacked accountability and drew resentment from the peasants.<sup>59</sup>

Lack of access to education became an increasing source of grievance for the peasantry. Peasants migrated to urban areas seeking out education to take away the elites monopoly on Spanish, reading and writing in order to provide opportunity for upward mobility.<sup>60</sup> In 1969, the military government attempted to restrict free high school education to students with passing grades, and caused the peasants of Ayacucho to create a social movement that defended free education.<sup>61</sup> In this instance, the government heeded to the desires of the people. Although such movements caused the government to discontinue such attempts at limiting education, it did not motivate the government to improve the education opportunities for the peasants in the rural areas. For the peasantry, education continued to provide upward mobility, remained highly desired and became the catalyst for many to migrate to the city in order to provide brighter future and more opportunities for their children.<sup>62</sup>

However, migration did not meet the expectations of many of the Peruvians. Once in the city, the Peruvians found themselves forced to work in the extralegal sector. The migrant's inability to receive legal recognition and public services (light, water, sewage, transport, and education) from the government caused them to create community organizations that employed an arsenal of pressures, from marches to bribes, in order to stimulate government action.<sup>63</sup> The government's inability to respond to the basic needs of their citizens often led to individuals

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<sup>59</sup> Ronald H. Berg, "Peasant Responses to Shining Path in Andahuaylas," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 120.

<sup>60</sup> Degregori, *The Shining Path of Peru*, 60.

<sup>61</sup> Ibid., 52.

<sup>62</sup> Hernando de Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (New York: Basic Books, 2000), 81.

<sup>63</sup> Michael L. Smith, "Shining Path's Urban Strategy: Ate Vitarte," In *The Shining Path of Peru*, edited by David Scott Palmer (New York: St. Martin's Press, 1994), 155.

forming local solutions outside the legal domain. Consequently, since the government did not sanction such local solutions, the government viewed such actions as illegal. However, a distinction must be drawn between what is truly illegal and extralegal.

## **Legal and Extralegal Activity**

Legal economic activities consists of economic activities occurring within a state that the state permits and governs by law. Extralegal activity consists of any activity that does not fall within the realm of legally sanctioned activity by the government. Black market activities or underground activities are additional terms used for extralegal activity that occurs outside of the law of the state. Regardless of the term used, such activity persists around the world and provides a source of income for many individuals. States often have the misconception that the extralegal sector exists only to provide cover for those avoiding taxes. Extralegal activity does not always equate to illegal activity. For example, when a government fails to provide a service such as public transportation for a community, entrepreneurs will often step in to fill the need. However, once the state changes the law to prohibit such activity, the extralegal activity now becomes illegal from the purview of the state.

Additionally states wrongly believe that solutions to land titling problems lie with building better databases, or that the current laws are sufficient, or the costs of compliance are at an acceptable level.<sup>64</sup> States should search for inclusive solutions and must understand the necessity of high-level political leadership to incorporate extralegal arrangements. When states fail to fully understand the extralegal sector's causes and effects, the existing grievances are further exacerbated. While severe problems exist with extralegal activity, individuals charged with reforming the system must understand that macroeconomic reforms are not enough.<sup>65</sup> Even if the macroeconomic reforms meet international standards, it does not equate to sustained

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<sup>64</sup> de Soto, *The Mystery of Capital*, 154.

<sup>65</sup> Ibid., 210.

economic growth in a society. Each state provides a unique set problems that require a distinctly different approach from other states. For example, until the recent entrepreneur expansion that changed the entire economy, India exemplified how state guidance hindered economic growth.<sup>66</sup> Although India followed a protectionist industry-building strategy for about fifty years, true economic growth did not occur until they were exposed to freer trade.<sup>67</sup> In the majority of cases, a heavy-handed, centralized approach to economic growth undermines entrepreneurial ability to create growth.

## **Economic Growth**

The majority of states desire to increase their economic growth. Although onerous economic policies often reduce such growth, this does not mean that economic policies lack merit. Prudent fiscal and monetary policies keep inflation low, prevents economic downturns, and fuels economic growth.<sup>68</sup> States reduce grievances by facilitating economic growth opportunity. When a state lacks economic opportunity, they are prone to political instability and backlashes.<sup>69</sup> It is important not to confuse economic growth with economic activity. Economists typically measure the economic growth of a country by the increase or decrease of the gross domestic product (GDP) that traditionally comprises a country's output of goods and services.<sup>70</sup> However, GDP only measures legal activities and fails to account for the majority of economic activities in non-Western states. This aspect provides one of the greatest opportunities for a state to change their economy. States can transform their economy through facilitating an environment that encourages economic growth in the legal economy. Key elements that facilitate

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<sup>66</sup> Baumol, Litan, and Schramm, 143.

<sup>67</sup> Reinert, 47.

<sup>68</sup> Baumol, Litan, and Schramm, 6.

<sup>69</sup> Ibid., 25.

<sup>70</sup> Baumol, Litan, and Schramm, 15.

growth for entrepreneurs are the ability to easily form a business and the legal enforcement of property and contract rights.<sup>71</sup>

## Law

The importance of law to encouraging economic growth cannot be overstated. In developing countries, laws often focus on protecting ownership and opportunities for a small group of elites.<sup>72</sup> For the majority, laws determine if they work within the formal sector or are forced to operate in the extralegal sector. Individuals in developing countries continually evaluate the cost of access to and the cost of remaining within the formal sector.<sup>73</sup> States should not arbitrarily create or enforce laws that only benefit the few. The state's laws must represent the society and their grievances. When a state understands the true sources of societal grievances, it is better prepared to create effective and unbiased law. Such laws reflect what is occurring in society and provide incentives for people to abide by the law.<sup>74</sup>

When a state faces rapid changes associated with mass migration to urban areas, the state often becomes overwhelmed and needs to re-evaluate its laws. The complex nature of these societal changes requires effective legal institutions able to enact changes in a timely manner. Peru provides an excellent example of the importance of creating effective laws and how a state must discard ineffective ones. In Peru's case, the debilitating laws of mercantilism sought to regulate every issue, every transaction, every property, but the state found efficient laws to replace the existing system and promote the desired ends.<sup>75</sup> Such a process is iterative and emerges unpredictably.

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<sup>71</sup> Ibid., 7.

<sup>72</sup> de Soto, *The Mystery of Capital*, 62.

<sup>73</sup> de Soto, *The Other Path*, 132.

<sup>74</sup> de Soto, *The Mystery of Capital*, 176.

<sup>75</sup> de Soto, *The Other Path*, 238.

## The Formal Sector

Commanders and planners must understand the importance of enabling and assisting individuals to operate within the formal sector of a state's economy. When individuals operate within the formal economy, their assets become live capital that is recognized and used globally. Formal property provides a primary mechanism to increase a state's economic growth. When the state's formal sector recognizes property, it effectively protects ownership, secures transactions, and encourages citizens in advanced countries to respect titles, honor contracts, and obey the law.<sup>76</sup> Although protection of ownership is important, the key aspect of the formal property lies in the ability to represent something other than its physical state. The ability of an individual to leverage property provides a catalyst that generates economic growth. In essence, formal property improves the flow of communications about assets and their potential.<sup>77</sup>

## The Informal Sector (the excluded)

Individuals existing in the extralegal sector do not enjoy the protections of the law. In Peru, the existing dominant groups in the legal sector viewed the new migrants to urban areas as competition. To limit the competition from such migrants, these dominant groups used Peru's legal institutions to bar migrants from establishing social and economic activities, sought means to maintain the elite privileges, and isolated the peasants in rural areas.<sup>78</sup> When individuals realize that the laws do not support their needs and excludes them from participation, they invariably seek alternatives to the legal system that provides protection.

The Peruvian economist, Hernando de Soto, describes informality as existing “when individuals and firms carry out economic activities that are inherently constructive – such as building homes, selling goods and services, and so on – but in ways that are technically illegal

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<sup>76</sup> de Soto, *The Mystery of Capital*, 55.

<sup>77</sup> Ibid., 59.

<sup>78</sup> de Soto, *The Other Path*, 11.

because they lack the requisite official approvals, licenses, or, in the case of land, titles.”<sup>79</sup> In many countries, the extralegal sector provides the majority of economic activity by its citizens. In fact, the International Labor Organization reports that during 1990s, eighty-five percent of all new jobs in Latin America and the Caribbean were created in the extralegal sector.<sup>80</sup> Although the extralegal assets of individuals become dead capital and lose the ability to generate economic growth in the legal arena, the cost associated with obeying the law are too onerous and outweigh any benefit of working within the legal sector. However, options do exist for individuals charged with creating economic growth. The United States’ expansion into the West provides an example of a state generating economic growth by successfully incorporating the extralegal sector. Although analysis of Western expansion does not provide an exact parallel, history reveals that when those in power accept and ratify established extralegal contracts, they provide a way to successfully transition from the extralegal to the legal sector.<sup>81</sup> This does not imply that legal systems should look to absorbing all extralegal arrangements. Rather, voluntary compliance will only occur if the system is relevant and efficient.<sup>82</sup>

## **Social Contract**

In creating a system that engenders compliance, the state absorbs social contracts into the legal sector and creates a national social contract with its citizens. To accomplish a national social contract, the state must understand the beliefs, desires, intentions, customs, and rules that are contained in these local social contracts.<sup>83</sup> Through this understanding, the state can begin to transition individuals into the legal sector. By creating a legal and political bridge from existing

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<sup>79</sup> Baumol, Litan, and Schramm, 75.

<sup>80</sup> de Soto, *The Mystery of Capital*, 69.

<sup>81</sup> Ibid., 174.

<sup>82</sup> de Soto, *The Other Path*, 245.

<sup>83</sup> de Soto, *The Mystery of Capital*, 157.

extralegal arrangements into a new social contract, the state gains the support of the people and individuals enjoy the benefits under formal law. The new contract brings the extralegal into the legal framework and gives them a stake in the capitalist system. However, this is a major political task since it tampers with the status quo.<sup>84</sup>

A state failing to incorporate the extralegal sector within its borders exposes itself to potential internal threats. Since extralegal assets are extremely hard to move without being connected to the legal sector, individuals have to rely on their extralegal social contracts. This reliance upon extralegal social contracts causes individuals to view the law and the government that was trying to enforce the law, as hostile to their interests.<sup>85</sup> It is extremely dangerous for a government to rely on established laws that exclude a significant portion of its populous. Failure to incorporate the excluded provides an opportunity for radical and subversive individuals and groups to gain the excluded's support, by providing asset protection, championing their causes, and providing a violent alternative to their present situation. Extralegal activity is not inherently subversive to the state. However, when the state limits the opportunities to only the politically well-connected, fatalism and despair occur, causing emigration or revolution.<sup>86</sup>

## Costs

People naturally follow rules that protect their assets. When the legal order fails to keep pace with economic and social upheaval, people invent informal, ad hoc business arrangements that do not always best serve their interests.<sup>87</sup> People tend to follow the laws that directly protect their assets. Hernando de Soto noticed that when laws were consensual, extralegal groups

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<sup>84</sup> Ibid., 188.

<sup>85</sup> de Soto, *The Other Path*, xxi.

<sup>86</sup> Ibid., 234.

<sup>87</sup> de Soto, *The Mystery of Capital*, 71.



preferred the formal titles over continuing previous arrangements.<sup>88</sup> This results from the cost associated with the extralegal sector. Contrary to popular thought, when individuals build a house outside the legal process, they pay a very high price for the land they occupy.<sup>89</sup> Additionally, any investment made to build or improve on that piece of land becomes dead capital since it exists in the extralegal sector. Both the individual and the state lose when this occurs. Hernando de Soto calculated that approximately \$9.3 trillion worth of real estate is held, but not legally owned, in the third world and former communist countries.<sup>90</sup> The primary reasons for individuals to hold their assets outside the legal sector stems from their inability to pay the costs of obtaining property. These are high costs in both time and money. Prior to changes in the government, it took a Peruvian more than three hundred days (working six hours a day), thirty-two times the monthly minimum wage, and seven hundred and twenty-eight bureaucratic steps to have an asset set up in the legal sector.<sup>91</sup>

## Capital

To obtain capital from their assets, an individual cannot remain in the extralegal sector. The importance of understanding how capital drives economic growth is vital when conducting expeditionary economics. Economists generally define “capital” as that part of a country’s assets that initiates surplus production and increases productivity.<sup>92</sup> Understandably, this can be difficult for those outside the field of economics to visualize. Capital is not money or accumulated stock of assets, but the potential it holds for new production.<sup>93</sup> An asset cannot be easily leveraged if it does not exist legally. One cannot put up their house as collateral for a loan

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<sup>88</sup> Ibid., 176.

<sup>89</sup> de Soto, *The Other Path*, 26.

<sup>90</sup> de Soto, *The Mystery of Capital*, 35.

<sup>91</sup> Ibid., 190-191.

<sup>92</sup> Ibid., 41.

<sup>93</sup> Ibid., 44.

if the bank is unsure of the legality of the asset. Therefore, capital can be seen as a title, a security, a contract, or other such record that represents the asset.

This is why capitalism works in the West and has difficulties elsewhere. Imitating capitalism by imitating Western economics through macroeconomic or structural reforms does not create wealth. Rather, states need to produce capital, which requires a legal property system.<sup>94</sup> This formal property system should represent assets in a way to allow individuals to understand each other, make connections, and synthesize knowledge about the assets to enhance productivity. Although many entrepreneurial individuals already possess the assets they need for success in a capitalistic system, the major stumbling block that keeps the rest of the world from benefiting from capitalism is its inability to produce capital.<sup>95</sup>

## **The Importance of Entrepreneurs**

Once the state provides mechanisms to unlock the economic potential of extralegal assets, entrepreneurs can tap into trillions of dollars of real estate in order to produce, secure, or guarantee greater value in the expanded market.<sup>96</sup> The key for the success of economic growth in the state is unlocking the potential of entrepreneurs. Entrepreneurs are any entity, new or existing, that provides a new product or service or that develops and uses new methods to produce or deliver existing goods and services at lower cost.<sup>97</sup> Entrepreneurs assume a tremendous amount of risk and initiative when they migrate from a rural to an urban area. This, coupled with the ability to identify and satisfy other's needs, creates wealth from knowing how to use resources, not from owning them. This entrepreneurial ingenuity creates wealth on a vast scale far exceeding the holdings of the government, the local exchanges, and foreign direct

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<sup>94</sup> Ibid., 66.

<sup>95</sup> de Soto, *The Mystery of Capital*, 5.

<sup>96</sup> Ibid., 47-48.

<sup>97</sup> Baumol, Litan, and Schramm, 3.

investment; they are many times greater than all the aid from advanced nations and all the loans extended by the World Bank.<sup>98</sup> However, when the wealth exists in the extralegal sector, it is essentially dead capital. By transferring this dead capital into the legal domain, entrepreneurs can utilize the new resources to accumulate much more wealth. Although a local community may view the rapid accumulation of wealth by an entrepreneur as a source of friction within a community, entrepreneurs are the solution for economic growth.

Entrepreneurship triumphed in the West because the law integrated everyone under one system of property, giving them the means to cooperate and produce large amounts of surplus value in an expanded market.<sup>99</sup> Capitalism provides the system for entrepreneurs to succeed and provides individuals the incentive to take risks. Individuals are more likely to come up with and implement good ideas than any group of planners or experts, and the very “un-plannedness” of a free-market economy, which might seem to be a great weakness, turns out to be a great strength.<sup>100</sup> The global economy is not a “zero sum game” where some countries “win” and others must “lose.”<sup>101</sup>

## **Failure and Success of Development Economics**

Countries and organizations with the best of intentions to improve the state’s economics fail on a regular basis. Many development economists tout that their list of requirements provides states with a plan that will create economic growth. However, the prerequisites that economists provide to states usually only apply to a small portion that have had some success. For instance, Jeffery Sachs lists the preconditions of basic infrastructure (roads, power, and ports) and human capital (health and education) coupled with foreign assistance as ingredients to create economic

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<sup>98</sup> de Soto, *The Mystery of Capital*, 34.

<sup>99</sup> Ibid., 71.

<sup>100</sup> Baumol, Litan, and Schramm, 87.

<sup>101</sup> Ibid., 187.

success.<sup>102</sup> Yet, economic growth occurs throughout the world without such preconditions or ingredients. Although no formula exists for the improvement of economic growth within a country, one can gain better understanding from looking at past successes and failures. Peru exemplifies a case where one can view both the successes and failures of economic development. By borrowing from this and other countries' successes and failures, commanders and planners can facilitate a better approach to future operations. The international community provides many examples that demonstrate the challenges and difficulties associated with changing a society's economic path. However, the two main obstacles to creating economic growth are free market reform and outside government intervention.

## **Free Market Reforms**

Financial markets provide a great source of free market efficiency and create opportunities for individuals to get rich by borrowing and investing.<sup>103</sup> While free markets do work, free markets reforms often fail as a result of the state taking a centralized approach to reform. The need to democratize the reform process constitutes one of the main challenges of institutional reform.<sup>104</sup> In order to get the local level to function in a free market requires the state to understand the reality at the local level. The ability to understand that poverty is a complicated tangle of political, social, historical, and institutional factors should cause a state to search for homegrown solutions.<sup>105</sup> This is where the system of state-driven capitalism differs from central planning. In centrally planned economies, the state picks the winners, owns the means of

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<sup>102</sup> Jeffrey D. Sachs, *The End of Poverty: Economic Possibilities for Our Time* (New York: Penguin Books, 2005), 3.

<sup>103</sup> Easterly, 76.

<sup>104</sup> Wise, 38.

<sup>105</sup> Easterly, 6.

production, sets all prices and wages, and provides no incentives for progress.<sup>106</sup> This does not insinuate that all state-driven capitalism economies work. For instance, oligarchic capitalism thrives on corruption and stymies economic growth. The attempted privatization in Russia displays the failure of state-driven capitalism to incorporate a participatory process that that included homegrown solutions.<sup>107</sup> However, states can promote growth and move toward a healthy form of capitalism if they understand the complexities of their society.

The state must find out what works at the local level. Failure to do so leads to one of the three main problems that create opposition to free markets. First, free market reforms that do not regulate profit-seeking behavior, allows opportunists to benefit at the expense of others.<sup>108</sup> Such regulation can be extremely difficult in disparate societies. For example, the state must provide enough protection for the wealthy or they will not accept the reforms. However, if the poor are excluded, they will revolt. Checks and balances are as important to economic development as is the existence of free markets.<sup>109</sup> The second challenge to free markets is failing to understand the local custom and its effect on the existing, working extralegal arrangements. For example, when aid agencies recommend to build computer databases to catalogue land titles as a solution to land ownership conflicts, they fail to understand the local challenges and potentially create more problems. Complex problems do not present simple solutions. The last challenge to free markets are rapid introduction of reforms designed to change all the rules at once. This drastic change disrupts the established order and causes such turmoil that the weak new arrangements are

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<sup>106</sup> Baumol, Litan, and Schramm, 64.

<sup>107</sup> Joseph Stiglitz, *Joseph Stiglitz and the World Bank: The Rebel Within* (London, Wimbledon Publishing Company, 2001), 239.

<sup>108</sup> Easterly, 63.

<sup>109</sup> *Ibid.*, 77.

unable to make the free market work well.<sup>110</sup> An abrupt change to an economic system creates confusion and often causes individuals to revert to something more familiar.

Since the state does not have the ability to possess all the required information to create lasting change, all reforms are partial. Rather than trying to accomplish everything at once, policy makers need to pursue inclusive ways that give the majority access to the free market. Too often, policy makers believe that their role is complete once they stabilized and adjusted the macroeconomic level, allowing legal business and foreign investors to prosper and orthodox economists to control the treasury.<sup>111</sup> The exclusion of the majority through free market reforms leads to future problems. Policy makers need to advance with gradual, experimental steps toward free markets.<sup>112</sup> This allows individuals to adopt reforms that work and states to better adapt to the changing requirements.

## **Outside Intervention**

Many observers outside of the state do not always believe that the state is capable of righting its own ship. Outside intervention normally consists of either military invasion or foreign aid. Although liberals may prefer big state-led effort to fight global poverty and conservatives prefer benevolent imperialism to spread Western capitalism and subdue opposition to the West, neither type of intervention works.<sup>113</sup> Macroeconomic plans fail despite the best of intentions, when outsiders fail to understand local customs and challenges. When outside government intervention attempts to design a comprehensive reform for a country that creates

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<sup>110</sup> Easterly, 101.

<sup>111</sup> de Soto, *The Mystery of Capital*, 211.

<sup>112</sup> Easterly, 61.

<sup>113</sup> Ibid., 18.

benevolent laws and forms new institutions to make markets work, it actually tends to exacerbate the problem.<sup>114</sup>

Commanders and planners must strive to understand the true causes of the local economic climate. The United States government promotes economic development as a part of its global war on terrorism, but the military is often insulated from being able to understand local interests.<sup>115</sup> Lasting change only occurs through homegrown solutions that embody local customs. Historically, at best, the majority of interventions by the military, IMF, World Bank and others produce mediocre results for the host country. Remarkably, countries lacking outside intervention will normally develop themselves regardless of the perceived inability to create positive change.

For example, without outside intervention, foreign aid, or even international recognition, the breakaway Republic of Somaliland in the north of Somalia enjoys peace, economic growth, and democratic elections.<sup>116</sup> Finding solutions to one's own problem is often easier than finding workable solutions for others. Often it comes down to an individual's mindset. Renowned economist and microfinance advocate C. K. Prahalad stated that when outsiders "stop thinking of the poor as victims or as a burden and start recognizing them as resilient and creative entrepreneurs and value-conscious consumers, a whole new world of opportunity will open up."<sup>117</sup> The ability of a developing state requires homegrown local solutions able to link capital to a market economy. Only then will macroeconomic reforms begin to work.

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<sup>114</sup> Ibid., 100.

<sup>115</sup> Easterly, 312.

<sup>116</sup> Ibid., 335.

<sup>117</sup> C. K. Prahalad, *The Fortune at the Bottom of the Pyramid* (Upper Saddle River: Wharton School Publishing, 2006), 1.

## Failures in Peru

Sometimes, the lessons of what works and what does not are best learned through the failure of others. The history of Peru provides numerous examples of the failures of economic plans. Normally, these plans focus primarily on macroeconomic changes that need to occur. Plans such as *Peru's Path to Recovery* by Carlos E. Paredes and Jeffrey Sachs, describe utopian goals of “creating a sound, enduring macroeconomic environment in which resources are allocated efficiently and where the state can secure sufficient resources for redistribution to the poorest members of the society.”<sup>118</sup> In broad strokes, 20<sup>th</sup> century Peru has experienced four roles: market-supporting role under a primary-export-led development model prior to the Great Depression; development role during the post WWII era of import-substituting-industrialization (ISI); direct role during post-debt-crisis retreat; and back to the pre-ISI liberal state meant to bolster private initiative through property rights enforcement and the providing basic public goods.<sup>119</sup> In the realm of expeditionary economics, two areas from Peru's past show that well-intentioned plans can produce disastrous results. Although the intervention came from within, the period of military rule provides lessons for others attempting future expeditionary economics. Additionally, the numerous attempts at land reform exemplify how the concentrations of a state on causes of problems do not always produce desired effects.

The case of the Peruvian military government provides a unique example that deviates from other military governments. One of the greatest differences from other military governments stems from the reasons for the military coup. In 1968, the military leadership felt that the Peruvian government's lack of a coherent economic policy created economic disparity

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<sup>118</sup> Carlos E. Paredes and Jeffrey D. Sachs, “Introduction and Summary,” In *Peru's Path to Recovery: A Plan for Economic Stabilization and Growth*, edited by Carlos E. Paredes and Jeffrey D. Sachs (Washington: The Brookings Institution, 1991), 38.

<sup>119</sup> Wise, 18.



and caused political coalitions to unravel.<sup>120</sup> The military correctly assessed many of the issues with the government at that time and believed that the military possessed the ability to correct Peru's economic and political path. Prior to this decision by the military, a remarkable change occurred within the military that transformed them from the protectors of the country's elites to an organization that believed they were capable of correcting Peru's economic and political woes. This belief stemmed from the training military leaders completed such as the Economic Commission for Latin America and the Caribbean (ECLAC) sponsored courses on structuralist economics and exposure to the main writings of the early dependency school in the Peruvian National War College (CAEM) training programs.<sup>121</sup> From this experience and training, top officers viewed the country's highly underdeveloped political and economic structures as the main threats to national security.<sup>122</sup> This, coupled with poverty-related guerrilla uprisings of the mid-1960s, further reinforced the military's perception that a sweeping socioeconomic reform was essential.<sup>123</sup> Thus, the Peruvian military believed that the situation required and demanded their intervention.

The overall goals of the military government centered on achieving greater national economic integration and reducing Peru's dependence on the world economy through upgrading the state's administrative and personnel practices, faster economic growth and higher levels of employment, and tighter controls on foreign direct investment (FDI) in the extractive sectors.<sup>124</sup> Despite the lofty reformist goals of the military regime, its legacy was just the opposite. In the end, a main legacy of military rule was increased state-led excessive external borrowing, reckless

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<sup>120</sup> Ibid., 11.

<sup>121</sup> Ibid., 83.

<sup>122</sup> Wise, 83.

<sup>123</sup> Ibid., 85.

<sup>124</sup> Ibid., 96-97.

state-owned enterprise (SOE) expansion, heightened conflict between the state and domestic entrepreneurs, and the degenerating poverty and income distribution.<sup>125</sup>

Although the military was well educated and professionally trained, these traits did not translate to economic success for Peru. This lack of success occurred during a period where the military understood the economic problems of Peru. In an effort to address the major economic and political issues, the military took a deliberate state-driven development approach. Yet, many of the reforms did not succeed. For instance, the modern-sector industrial reforms did not quickly absorb the traditional sector into the national economy.<sup>126</sup> Additionally, agrarian reforms failed to work because the government did not accept that people have their own methods of using and exchanging land.<sup>127</sup>

One of the main causes for these failures rests with the use of military officers. Although the officers possessed high levels of education and training, the technical nature of the development program coupled with the managerial requirements did not match with such education and training. For instance, the efforts of a strategically placed military cadre to act quickly in transforming the political economy led to immediate structural imbalances, contradictory development outcomes, the failure to reconcile redistributive goals with the chosen model of capital accumulation, and an ambiguous stance toward domestic and foreign capital.<sup>128</sup>

Additionally, the placement of military officers with a highly capable corps of technocrats caused more problems. Problems manifested themselves in the hasty launch of the development effort, conspicuous lack of clear goals, and the built-in tensions of a convoluted management strategy. This ill-informed strategy merged military and civilian policy makers into

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<sup>125</sup> Ibid., 84.

<sup>126</sup> Ibid., 103.

<sup>127</sup> de Soto, *The Mystery of Capital*, 168.

<sup>128</sup> Wise, 86.

a top-down hierarchical relationship that operated within the civilian policy maker's bureaucratic turf.<sup>129</sup> Throughout this period, the military was often its own worst enemy. The military undercut its antioligarchic reforms and alienated the working and middle class that they were trying to help by granting generous industrial incentives and salary increases until the 1974 fiscal crunch.<sup>130</sup> These problems were not isolated incidents. For example, the military government lost the support of entrepreneurs by issuing the 1970 Job Stability Law granting workers virtual job tenure.<sup>131</sup> In the end of the military government era, every major approach the military took resulted in increased tensions. Heavy reliance on state-owned enterprises (SOEs) to develop the country failed because of the tension between the firm's pursuit of microeconomic investment goals and the central government's macroeconomic and social objectives.<sup>132</sup> Capital investment programs appeared to favor urban areas over the rest of the country. Debt-backed consumption reduced from borrowing for productive investments.

By the 1976 debt crisis, these competing policy approaches failed to support Peru's development goals and left the country's economy in disarray. Entrepreneurs certainly emerged no stronger from the experience of the 1970s, and workers emerged much better organized and able to articulate their interests.<sup>133</sup> It is difficult to overlook the distributional shortcomings of the military's program, including the propensity of social subsidies to favor town over country and the near exclusion of the jungle and sierra regions from the capital-investment program.<sup>134</sup> As in the 1970s and the early 1980s, the domestic debate over how to proceed with economic adjustment wavered between a draconian shock treatment and a more gradual approach to

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<sup>129</sup> Ibid., 92.

<sup>130</sup> Ibid., 94.

<sup>131</sup> Ibid., 94.

<sup>132</sup> Ibid., 107.

<sup>133</sup> Wise, 114.

<sup>134</sup> Ibid., 115.

stabilization.<sup>135</sup> The military's effort to reorganize society into benign classless units actually resulted in enhancement of class-consciousness and conflict.<sup>136</sup> The military's failure to promote equitable economic growth and mediate societal issues created opportunities for subversive groups to garner support. Although the military turned the government back over to civilian leadership in 1980, Peru's political and economic woes continued. The 1982 debt shocks led to a period of chronic financial insolvency and fiscal retrenchment which prompted a retreat from statist strategies to a more indirect mode of state participation in the 1990s.

## **Development Economics International Successes**

Historically, not all development economic efforts in creating economic growth within a country fails. Although Peru failed to create economic growth through many of its economic policies, other states succeeded using a seemingly similar approach. Chile experienced a seventeen-year military government that abandoned the ISI economic policies and followed a market strategy. The Chilean government provided political freedom to policy makers to experiment with market reform until they obtained the desired results.<sup>137</sup> This Chilean strategy allowed the state to sustain economic growth even after the 1982 debt shocks. The ability to experiment provides a state with one of the best tools for economic change. What works for one state does not become a panacea that works for another state. For instance, the failure of SOEs in Peru does not mean that economic success is impossible when a state supports SOEs. In China, SOEs produced tremendous success and helped drive China's economic growth. The reason for China's success with SOEs originates from their ability to use the SOEs when needed and then gradually reduce them while supporting the privatization of the Chinese economy. This support

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<sup>135</sup> Ibid., 175.

<sup>136</sup> Ibid., 96.

<sup>137</sup> Ibid., 30-31.

manifests itself through recognizing property rights and allowing villages to own and operate new firms.<sup>138</sup>

States creating economic growth normally follow a path unique to that state. Successful changes do not result from one state's imitation of another's economic path. The economic history of Western states provides plenty examples for states and international agencies to understand how successful economies occur. The primary factor for states to transition to capitalism originates with laws that adapt to the emerging needs of people. However, the history and process by which laws absorb the practices, customs, and norms of extralegals have been obscured by other historical events.<sup>139</sup>

Throughout United States history, in the absence of inclusive laws, individuals must create and agree upon extralegal rules. The United States government realized the difficulty of enforcing exclusive laws that did not work and the futility of making existing laws more stringent. Therefore, Congress gradually managed to integrate into one system the informal property rules created by millions of immigrants and squatters.<sup>140</sup> By creating laws that absorbed extralegal arrangements, Congress enabled individuals to become more productive and generate economic growth.

Many countries view those operating outside the legal realm as criminals. However, positive change occurs when states view the extralegal sector as providing an opportunity for the state to improve its economy. For example, in the Homestead Act of 1862, the United States government provided settlers with 160 acres of free land if the settlers agreed to develop the land. The government's actions essentially legalized existing extralegal practices that were occurring

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<sup>138</sup> Baumol, Litan, and Schramm, 56.

<sup>139</sup> de Soto, *The Mystery of Capital*, 109.

<sup>140</sup> *Ibid.*, 53.

for decades.<sup>141</sup> Even in the American Colonial period, authorities provided property rights to individuals who improved the land, paid taxes, and followed local arrangements among neighbors.<sup>142</sup> The efforts to embrace many of the settler's extralegal arrangements led the United States Congress to pass more than five hundred different laws to reform the property system between 1785 and 1890.<sup>143</sup> This exemplifies the effort it took to provide inclusive laws that created a powerful economic engine.

## **Peru's Successes**

In the 1990s, Peru provides another example of how states can create economic growth through multiple means. When the Alberto Fujimori administration emerged, fifty percent of the population lived in poverty, half of which lived in extreme poverty.<sup>144</sup> Many leading economists of the time proposed solutions for Peru to create economic growth. Top Peruvian economists teamed with Harvard professor Jeffrey Sachs to generate the macroeconomic plan called "A Plan for Economic Stabilization and Growth."<sup>145</sup> However, the Fujimori administration took a different path. In order to take the country out of hyperinflation and entice foreign investment, Fujimori enacted several macroeconomic reforms that eliminated government controlled prices and subsidies, introduced emergency taxes, established a managed floating-exchange-rate, and reduced tariffs on trade.<sup>146</sup> Although such measures created hardships among the most vulnerable in Peru, Fujimori made efforts to communicate the goals of the central government to discover the desires of the locals and address their needs. By creating the Programa de Emergencia Social

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<sup>141</sup> Ibid., 107-108.

<sup>142</sup> Ibid., 119.

<sup>143</sup> de Soto, *The Mystery of Capital*, 128.

<sup>144</sup> Wise, 183.

<sup>145</sup> Ibid.

<sup>146</sup> Ibid., 184-185.

(PES) and assembling organizations such as the Catholic Church and Non-governmental Organization (NGOs) to participate in the program, Fujimori established the central coordinating committee and local emergency committees that assisted in creating development solutions.<sup>147</sup> Such organizations provided a voice for grassroots leaders and contributed to the undermining of support for the Shining Path.

President Fujimori relied on market forces for much of the economic recovery. He resisted outside intervention and looked for ways to reform Peruvian society. Property reforms built respect for the law and alleviated many individual's grievances that feared the government's expropriation of their extralegally held land. The Fujimori government made it convenient for people to file complaints about excessive bureaucracy by establishing the Administration Simplification Tribunals. The televised tribunals allowed the people to directly examine improvements in different types of bureaucratic processes.<sup>148</sup> During this time, Peru provides an example of a state that became inclusive to its population. This inclusion also extended to coca farmers. Such inclusion benefitted the state and the farmers. The legal recognition of coca farmers resulted in information that helped the government eliminate many terrorist and drug trafficker sanctuaries.<sup>149</sup> Reducing bureaucracy, eliminating institutions that protect the few, creating agencies to support reforms, providing infrastructure and public services, all worked toward building a stronger economic growth machine.

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<sup>147</sup> Isabel Coral Cordero, "Women in War: Impact and Responses," In *Shining and Other Paths: War and Society in Peru, 1980 – 1995*, edited by Steve J. Stern (Durham: Duke University Press, 1998), 367.

<sup>148</sup> de Soto, *The Other Path*, xxviii.

<sup>149</sup> *Ibid.*, xxvii.

## **Emergence of Market Economy**

Economic systems are complicated, and no single policy prescription, even if precisely followed, is likely to be sufficient to ensure rapid, sustainable growth over time.<sup>150</sup> Generally, for a state to establish a market economy does not require destruction and rejection of existing arrangements. When intervening in a state's economic system, elites and bureaucracies who benefit from the previous system will resist change. However, in order to improve economic growth within a society, the excluded must be included in the legal system that has traditionally shut them out. The ability to gain acceptance from both groups is extremely difficult to do since most policy makers do not fully understand local level activities. No simple answer exists to bring both sides to a consensus. Creating redistributive expectations or establishing specific goals will exacerbate problems. The free market operates with only general goals.<sup>151</sup> By setting general goals, opportunities emerge where the state can integrate the informal institutions and provide the needed level of protection once made available by the extralegal sector. The state's challenge is to embrace the potential solutions that surface. Markets everywhere emerge in unplanned, spontaneous ways, adapting to local traditions and circumstances, and not through externally designed reforms.<sup>152</sup>

## **Importance of the Law over Other Variables**

Understanding the laws, economic policies, and practices that prevent inclusion provides the first step for a country to change its economic health. Recognizing the approach to take constitutes one of the most difficult aspects of expeditionary economics. Although commanders and planners should understand the historical background of successes and failures of economic intervention, such understanding often fails to provide a good guide for future problems. The

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<sup>150</sup> Baumol, Litan, and Schramm, 6.

<sup>151</sup> Easterly, 12.

<sup>152</sup> Easterly, 61.



responsibility for the macroeconomic policy management rests with the state. However, policies that worked in the past does not translate to the same policies working in the future. When prescribing past successful economic policies, the state assumes that the economies, to which they are applying these policies, will continue to behave or operate in fundamentally the same way as in the past or at least in similar fashion.<sup>153</sup>

Blaming the poor economic growth on historical factors is a similar fallacy as blaming its demise on cultural reasons. While cultural understanding is extremely important to successful expeditionary economics, culture should be viewed as an opportunity to generate economic growth instead of a cause of economic woes. However, David Landes of Harvard University Department of Economics claims that growth is primarily about culture and that some societies have hard-working, enterprising people whereas others do not.<sup>154</sup> This view embodies a very dangerous argument since such arguments concentrate on the differences between people and groups instead of what they have in common. For instance, all cultures have entrepreneurs. However, not all cultures accept such groups and fail to encourage their growth. True, some cultures tend to focus on protecting elites, but this is common across most cultures and must be handled both politically and legally. The legal reform process required to bring the extralegal entrepreneurs into one official legal framework is essentially a cultural exercise: adapting Western market and corporate law to the vibrant cultures and customs of the developing state's new entrepreneurs.<sup>155</sup> This change in culture does not transpire overnight. It takes time for individuals to recognize how cultural arguments provide a shelter for the effects of good political institutions and laws. The arguments made individuals who continue to use culture as a reason for the state's economic success or failures fall short. Prior to the "East Asian miracle," many

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<sup>153</sup> Baumol, Litan, and Schramm, 43.

<sup>154</sup> David S. Landes, *The Wealth and Poverty of Nations: Why Some Are So Rich and Some So Poor* (New York: W.W. Norton, 1999), 516-517.

<sup>155</sup> de Soto, *The Other Path*, xxxvii.

economists blamed a Confucian culture for the lack of economic success in East Asia, but post-miracle, touted such culture as the catalyst for economic success.<sup>156</sup> All culture can become supportive of economic development. Much behavior that is attributed to cultural heritage is not the inevitable result of people's ethnic or idiosyncratic traits but of their rational evaluation of the relative costs and benefits of entering the legal property system.<sup>157</sup>

The importance of inclusive laws cannot be overemphasized. American economists, Douglass North and Oliver Williamson, argue that favorable economic performance requires the following: a market grounded in a sound set of domestic institutions that includes formal rules such as statutes, common laws, regulations, and property rights embodied in the judicial system; informal rules in the way of conventions, norms, and self-imposed codes of conduct; and a wide range of state and societal organizations.<sup>158</sup> Successful systems embrace many of the social contracts pieced together by knowledgeable people familiar with the local environment. One of the main legal obstacles originates from the law's inability of the official law to maintain pace with popular initiative, causing the government to lose control.<sup>159</sup>

To improve the law to support economic revival, one of the greatest hurdles a state must overcome stems from the legal profession. Although the legal profession perfects all the artifacts of formal property: titles, records, trademarks, copyrights, promissory notes, bills of exchange, patent rights, and shares of corporate stock, few lawyers understand the economic consequences of their work.<sup>160</sup> The political actions that embrace grassroots solutions are vital to create inclusive laws that the majority accepts. Therefore, the state must employ a careful strategy for

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<sup>156</sup> Ha-Joon Chang, "The East Asian Development Experience," In *Rethinking Development Economics*. edited by Ha-Joon Chang (London: Anthem Press, 2003), 119.

<sup>157</sup> de Soto, *The Mystery of Capital*, 226.

<sup>158</sup> Wise, 4.

<sup>159</sup> de Soto, *The Mystery of Capital*, 149.

<sup>160</sup> de Soto, *The Mystery of Capital*, 199.

dealing with the legal profession if the government moves to integrate the extralegal sector. By viewing extralegal individuals as enterprising rather than criminals, the state will begin to integrate them into the formal legal system. The Western experience shows that inclusion is a threefold task: find the real social contracts on property, integrate them into official law, and craft a political strategy that makes reform possible.<sup>161</sup>

When Peru made important parts of the law accessible for all people, the state deprived the Shining Path of fertile ground for its insurgency. In economic matters, people do not rebel because they are poor, rather because they are excluded from the system.<sup>162</sup> While courts can help promote inclusive economic activity, they are not the sole answer to improving the system. The costs of legal action for small transactions often outweigh the benefits gained from the protection of property through the legal process.<sup>163</sup> When politicians respond to society's needs and discover ways to establish more honest courts, judges, and police, economic growth becomes possible.<sup>164</sup>

## Conclusion

Commanders and planners face incredible challenges when they engage in expeditionary economics. This immense undertaking requires contextual understanding of the causes of grievances within the state. With this understanding, commanders and planners can influence a state to change laws and economic practices. On account of the political nature of creating change that produces economic growth, the state's leadership cannot focus solely on meeting the demands of the poor or excluded. However, change does occur when the state takes the perspective of the poor, co-opts the elite, and addresses exclusive law and technical bureaucracies

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<sup>161</sup> Ibid., 151.

<sup>162</sup> de Soto, *The Other Path*, xxxv.

<sup>163</sup> Ibid., 177.

<sup>164</sup> Easterly, 117.

that exist only to further the current economic system.<sup>165</sup> This process requires knowledge of not only how markets work from the macroeconomic level, but also entails searching the local level for the social norms that create the extralegal agreements. By incorporating these agreements, the state protects property and person and undercuts the extralegal arrangements that undermine the respect for the rule of law. If the state fails to protect property and person, history shows how even a murderous Mafia can meet a genuine social need when law and order collapse.<sup>166</sup>

This does not imply the necessity to incorporate all local arrangements. In fact, many such arrangements will only benefit the few and therefore, negatively effect economic growth. Instead, the state must utilize what actually works within the extralegal arrangements in order to get extralegal individuals to voluntarily adapt to the new circumstances.<sup>167</sup> The extreme entrepreneurial abilities of individuals in the extralegal sector provide everything from basic road infrastructure, water supply, sewage systems, and electricity to actually administering markets, justice, and laws. When the state creates quality laws that enable the inclusion of the majority of its citizens, the entrepreneurs become a part of a global market that increases the state's economic growth. Politicians should guide the change and give it an appropriate institutional framework so that the people can properly use and govern the changed environment.<sup>168</sup>

When the state's goal is to become a member of the modern market economy, the state's leadership must create a system that gives entrepreneurs access to the legal system. Such a system requires incorporating successful extralegal processes along with ensuring simple entry cost into the new system in both time and money. Additionally, transparency is a crucial aspect to the system's success. In Peru's case, the Fujimori government televised individual cases that

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<sup>165</sup> de Soto, *The Mystery of Capital*, 190.

<sup>166</sup> Easterly, 89.

<sup>167</sup> de Soto, *The Other Path*, 245.

<sup>168</sup> *Ibid.*, 240.

showed how the current law changed. The strength of the press and judiciary is important in order to effectively scrutinize the government's actions. However, this is not always possible at the onset of creating change that increases economic growth.

The challenge for those conducting expeditionary economics is to encourage and influence the state to create legal and institutional systems that reflect a new reality. This new reality allows the fledgling economy that spontaneously emerges to function in an orderly fashion and enables competitive formal businessmen and merchants to produce with security.<sup>169</sup> Each state has a unique and complex history, culture, and set of grievances that may seem similar to other situations. However, each state requires an approach that is specific and particular to that state. Commanders and planners should not view aspects culture and history as a barrier to economic development. Rather, they should incorporate such aspects with the intention of supporting economic development. In order to provide successful and workable solutions, it is important to decentralize lawmaking and decision making to local governments. By transferring these responsibilities to local and regional governments, they are better able to enact beneficial laws since they are closer to the local issues, struggles and grievances. Regardless of the method used to create inclusive laws, the central government must find the means to incorporate existing arrangements. The United States Congress provides an excellent historical example of how the United States incorporated land laws through an iterative process of over five hundred laws in a span of over a hundred years. Although not perfect, researchers purport that the bottom-up approach to law is superior for economic development to more top-down approaches.<sup>170</sup>

The subject of expeditionary economics covers an incredible amount of areas for a state. The right plan does not exist and is itself a symptom of a misdirected approach.<sup>171</sup> Although no

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<sup>169</sup> de Soto, *The Other Path*, 245-246.

<sup>170</sup> Easterly, 97.

<sup>171</sup> *Ibid.*, 5.

panacea exists to expertly guide the military in the conduct of expeditionary economics, contextual understanding of the underdeveloped state remains essential. Prior to conducting expeditionary economics in a state, commanders and planners can garner information from aid agencies that have individuals who have gained experience in a particular local setting on a particular problem. These are the individuals who can describe what is and is not working within a local environment. Still, this remains only one piece of an extremely complicated economic problem. Regardless what the military may think of local grievances, the institutions work most effectively, if at all, if they are homegrown. With contextual understanding, the military through expeditionary economics, can assist a state to establish a system that generates an engine of economic growth.

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